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FEDERAL COMMUNICATIONS COMMISSION

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In the Matter of:

COMMON CARRIER BUREAU FORUM:

COMBINATIONS OF UNBUNDLED
NETWORK ELEMENTS

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of:)
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COMMON CARRIER BUREAU FORUM:)
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COMBINATIONS OF UNBUNDLED)
NETWORK ELEMENTS)

Room No. 847
FCC Building
1919 M Street, N.W.
Washington, D.C.

Thursday,
June 4, 1998

The parties met, pursuant to the notice, at
9:34 a.m.

APPEARANCES:

On behalf of the Federal Communications
Commission:

A. RICHARD METZGER, JR.
MICHAEL PRYOR
MELISSA NEWMAN
JAKE JENNINGS
CAROL MATTEY
JORDAN GOLDSTEIN
KATHERINE SCHRODER

I N D E X

<u>STATEMENT OF:</u>	<u>PAGE</u>
<u>Panel One:</u>	
KEITH TOWNSEND, DIRECTOR OF LEGAL AND REGULATORY AFFAIRS AND SENIOR COUNSEL, UNITED STATES TELEPHONE ASSOCIATION	8
JUDITH LEVINE, EXECUTIVE DIRECTOR, MASS MARKETS LOCAL MARKETING, MCI TELECOMMUNICATIONS CORPORATION	12
GERRY SALEMME, SENIOR VICE-PRESIDENT, EXTERNAL AFFAIRS AND INDUSTRY RELATIONS, NEXTLINK COMMUNICATIONS, INC., o/b/o ASSOCIATION FOR LOCAL TELECOMMUNICATIONS SERVICES	17
<u>Panel Two:</u>	
JEFF OWENS, EXECUTIVE DIRECTOR, REGULATORY STRATEGY, U.S. WEST, INC.	27
BRYAN KENNEDY, VICE-PRESIDENT CLIENT SERVICES, CON-X CORPORATION	30
ROBERT V. FALCONE, DIVISION MANAGER, LOCAL SERVICES DIVISION, AT&T CORPORATION	33
FRANK LAURIA, VICE-PRESIDENT OF SALES AND MARKETING, COMMTECH CORPORATION	38
<u>Panel Three:</u>	
DAN POOLE, DIRECTOR OF NETWORK PLANNING AND ENGINEERING, SOUTHWESTERN BELL TELEPHONE COMPANY	60
JOHN LENAHAAN, ASSISTANT GENERAL COUNSEL, AMERITECH CORPORATION	65
ROCKY N. UNRUH, MORGENSTEIN & JUBELIRER, COUNSEL FOR LCI INTERNATIONAL TELECOM CORPORATION	71
GARY BALL, VICE-PRESIDENT OF REGULATORY POLICY, WORLDCOM, INC.	74

I N D E X

<u>STATEMENT OF:</u>	<u>PAGE</u>
<u>Panel Four:</u>	
LEONARD CALI, GENERAL ATTORNEY, LAW AND PUBLIC POLICY, AT&T CORPORATION	104
JOSEPH GILLAN, TELECOMMUNICATIONS CONSULTANT, o/b/o COMPETITIVE TELECOMMUNICATIONS ASSOCIATION	109
DONALD C. DAVIS, ASSISTANT VICE-PRESIDENT, INDUSTRY POLICY, INTERMEDIA COMMUNICATIONS, INC.	114
WILLIAM N. STACY, ASSISTANT VICE-PRESIDENT, SERVICES FOR INTERCONNECTION OPERATIONS DEPARTMENT, BELLSOUTH TELECOMMUNICATIONS, INC.	119
MICHAEL GLOVER, ASSISTANT GENERAL COUNSEL, BELL ATLANTIC CORPORATION	126
<u>Panel Five:</u>	
WILLIAM J. CELIO, DIRECTOR, COMMUNICATIONS DIVISION, MICHIGAN PUBLIC SERVICE COMMISSION	163
PEGGY RUBINO, SENIOR VALUATION ENGINEER, NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE	171
DONNA NELSON, ASSISTANT DIRECTOR OF LEGAL, OFFICE OF REGULATORY AFFAIRS, LEGAL DIVISION, TEXAS PUBLIC UTILITY COMMISSION	174
ACCOMPANIED BY: NARA SRINIVASA	
BRAD RAMSAY, ASSISTANT GENERAL COUNSEL, NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS	177

Meeting Began: 9:34 a.m.	Hearing Ended: 3:35 p.m.
Recess Began: 12:06 p.m.	Recess Ended: 1:33 p.m.

P R O C E E D I N G S

MR. METZGER: Good morning. For those of you who are not able to find seats, there is overflow seating in Room 535 and in Room 315 where you can see this on closed circuit.

I want to welcome all of you for coming this morning. I particularly want to welcome and thank the panelists for coming and participating in this forum on such short notice.

Since January, as I assume all of you know, the Common Carrier Bureau has been meeting with Bell companies, new entrants and others who have an interest in the issues surrounding the statutory requirements set forth in Section 271.

As part of that ongoing dialogue, the Bureau is hosting this public forum to discuss a particularly difficult Section 271 issue, which is also a 251 issue, which is how a Bell company may satisfy the checklist requirement that it provide non-discriminatory access to unbundled network elements in a manner that allows new entrants to combine them.

Last year, the U.S. Court of Appeals for the Eighth Circuit determined that new entrants may provide telecommunications services through the use of combinations of network elements. The Court concluded, however, that

1 incumbent local exchange carriers are not required to
2 combine the elements for new entrants.

3 In the wake of the Eighth Circuit decision,
4 incumbent LECs have taken the position that collocation is
5 the only method for combining network elements that is
6 authorized by the Act. New entrants have vigorously
7 disputed this view.

8 This forum should allow representatives from
9 different segments of the telecommunications industry to
10 discuss the legal requirements relating to combining network
11 elements. Fundamentally, we are here to discuss what is
12 consistent with the Eighth Circuit's decision and satisfies
13 the non-discrimination standard in Section 271. This public
14 forum is intended to provide an opportunity for an open and
15 frank exchange of views on the complicated legal, technical
16 and economic issues that concern this question.

17 We are pleased to have a diverse array of
18 representatives from all segments of the industry. We are
19 particularly pleased to have representatives from state
20 commissions here to share their views on how the Bell
21 companies may provide unbundled network elements in a manner
22 that allows new entrants to combine them. Like so many
23 other aspects of the 1996 Act, the devil is in the details,
24 and the state commissions have been extremely busy over the
25 last year identifying more demons than they probably thought

1 possible.

2 Again, I want to express my thanks to all the
3 panelists for making time in their busy schedules to
4 participate in this forum. I look forward to an informative
5 and productive debate, and now I will turn this over to
6 Carol Matthey, Chief of the Policy and Program Planning
7 Division, who has organized and put this forum together on
8 such short notice.

9 Thank you all for coming.

10 MS. MATTEY: Good morning. I also want to thank
11 everyone for coming here this morning. First I would like
12 to give you an outline of what we intend to do today. We
13 have an ambitious schedule, and we have a lot to talk about.

14 Today's forum will have five panels. The first
15 panel is intended to provide an overview of the importance
16 of combinations of network elements as a competitive entry
17 strategy. The second panel, which is largely a technical
18 panel, will examine the development and availability of
19 different methods for combining network elements.

20 Panel three will explore the legal, technical and
21 economic issues surrounding the use of collocation as a
22 method for combining network elements. The fourth panel
23 will discuss other methods for combining network elements,
24 such as direct access, electronic methods for combining
25 network elements and having the BOC combine the elements for

1 a separate charge. The fifth panel will present the state
2 perspective on these issues.

3 Before we begin, I would like to establish the
4 ground rules for the discussion. First, the panelists will
5 have an opportunity to make very brief opening remarks,
6 three to five minutes, and we will be enforcing those time
7 limits. After each panelist has made an opening statement,
8 the Bureau will direct questions to the panelists. We ask
9 the panelists to keep their responses as succinct as
10 possible. Other panelists will have an opportunity to
11 respond again briefly.

12 Time permitting, we then will take questions and
13 comments from the audience. If we are unable to get to all
14 of the questions from the audience, we encourage people to
15 submit written questions to the Bureau that we can consider
16 as this dialogue continues.

17 Throughout, the panelists should relate their
18 remarks to the statutory standards set forth in Section 271
19 under which the Commission will be evaluating a Bell
20 company's provision of access to unbundled network elements.

21 Finally, I want to note that this forum is subject
22 to the Commission's ex parte rules, and we will be placing a
23 transcript of the discussion in each of the open Section 271
24 dockets.

25 Again, thank you for coming. Before turning to

1 the first panel, I would like to introduce those who have
2 helped put together this forum, specifically Jake Jennings
3 on my right, Katherine Schroder and Jordan Goldstein on my
4 left.

5 I also want to introduce my deputies, Melissa
6 Newman, who is sitting here, and Michael Pryor, who is
7 sitting back there, who will be sitting in as a moderator as
8 the day progresses.

9 Thank you, and let's get started.

10 The Act permits new entrants to provide
11 telecommunications service using combinations of unbundled
12 network elements. For example, a new entrant may combine
13 the loop, switch and transport or may combine the loop and
14 transport to provide service.

15 Our first panel this morning will address the
16 significance of combinations of network elements as an entry
17 strategy into the local market. Participating on this panel
18 this morning are Keith Townsend from the U.S. Telephone
19 Association, Judith Levine from MCI, and Gerry Salemm from
20 NEXTLINK, representing the Association of Local
21 Telecommunications Services.

22 We will start off with Keith once he has a chance
23 to get a glass of water.

24 MR. TOWNSEND: I am Keith Townsend. I am Director
25 for Legal and Regulatory Affairs and Senior Counsel for the

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1 United States Telephone Association. I am pleased to
2 participate in this Commission forum. USTA is the principal
3 trade association of the local exchange carrier industry
4 representing more than 1,200 members nationwide.

5 As everyone is aware, the Telecommunications Act
6 of 1996 was signed into law just over two years ago. The
7 Commission's initial orders implementing the Act are less
8 than two years old. Through the energetic and enthusiastic
9 support of incumbent LECs, competition in the local exchange
10 is growing at unprecedented levels.

11 As USTA's president and CEO, Roy Neal stated in
12 his remarks during the Commission's January 29, 1998, en
13 banc hearing on local competition, "Thousands of
14 interconnection agreements have been negotiated. Hundreds
15 of collocation arrangements exist, and the CLECs have been
16 certificated in every state and are taking market shares,
17 especially high end business customers."

18 As Solomon Smith Barney analyst Jack Grubman
19 confirmed in a report on May 6, CLECs added more than
20 498,000 new business lines during the first quarter of 1998,
21 as compared to 461,000 net business lines for the baby Bells
22 during the same period.

23 According to Mr. Grubman, the non-AT&T long
24 distance competitors did not have more incremental minutes
25 than AT&T until 1986, a full ten years after MCI carried its

1 first switched long distance minute. Mr. Grubman further
2 stated that if one takes the obvious logistical extension of
3 this, this means that the 50 percent loss of market share
4 that AT&T saw from 1986 through 1996 could be replicated in
5 the local markets in a much quicker time period.

6 Further evidence of the explosive growth in local
7 competition is the value that Wall Street and the investment
8 community places on the CLEC industry. According to the
9 Supreme Court brief filed by ALTS on May 18, which cites a
10 report from Bear Stearns dated March, 1998, local
11 competitors have raised over \$14 billion for competitive
12 investments since the passage of the Act. Thus, the CLECs
13 are a growth market with billions of dollars in
14 capitalization.

15 Remember, these developments have occurred in less
16 than two years since the Commission issued its first orders
17 implementing the 1996 Act. Without question, the tremendous
18 growth in local competition could not have been achieved
19 absent ILECs implementing the requirements of the Act.

20 The 1996 Act provides for three means of
21 competitive entry. The CLEC uses its own facilities based
22 network and interconnects with ILECs. The CLEC purchases
23 ILEC unbundled network elements, combines them with their
24 own facilities to provide alternative telecommunications
25 services, and the CLEC can resell ILEC retail

1 telecommunications services.

2 The 1996 Act requires that new entrants have
3 access to ILEC UNEs on a non-discriminatory basis. The 1996
4 Act requires CLECs to combine UNEs into alternative
5 facilities based telecommunications services. The Eighth
6 Circuit Court has held that the Act does not require ILECs
7 to combine UNEs for CLECs. As the Court stated, "Despite
8 the Commission's arguments, the plain meaning of the Act
9 indicates that the requesting carriers will combine the
10 unbundled elements themselves."

11 The Act does not require the incumbent LECs to do
12 all the work. The last sentence of Subsection 251(c)(3)
13 reads, "An incumbent local exchange carrier shall provide
14 such unbundled network elements in a manner that allows the
15 requesting carrier to combine such elements in order to
16 provide such telecommunications services." The Court
17 concluded that this sentence unambiguously indicates that
18 requesting carriers will combine the unbundled elements
19 themselves.

20 The Court further stated, "Section 251(c)(3)
21 requires an incumbent LEC to provide access to the elements
22 of its network only on an unbundled, as opposed to a
23 combined, basis." Stated another way, Section 251(c)(3)
24 does not permit a new entrant to purchase the incumbent
25 LECs' assembled platforms of combined network elements or

1 any lessor existing combination of two or more elements in
2 order to offer competitive telecommunications services.

3 To permit such an acquisition of already combined
4 elements at cost base rates for unbundled access would
5 obliterate the careful distinctions Congress has drawn in
6 Subsection 251(c)(3) and (4) between access to unbundled
7 network elements on the one hand and the purchase at
8 wholesale rates of an incumbent's telecommunications retail
9 services for resale on the other.

10 What is equally clear is that the ILECs are
11 fulfilling their obligations as required by the Act. No
12 American industry or company, not even Microsoft, is under
13 the tremendous regulatory oversight and scrutiny that ILECs
14 receive from the Commission, state commissions, the DOJ with
15 respect to all BOCs Section 271 applications for in region
16 long distance authority, Congress and the investment
17 community regarding their day to day operations.

18 The 1996 Act is the law, and ILECs have been and
19 will continue to be in full compliance with that law. Thank
20 you.

21 MS. MATTEY: Judy?

22 MS. LEVINE: Thank you. Good morning. My name is
23 Judy Levine. I am here representing MCI. In particular, my
24 role within the company is to focus on local service
25 competition for the residential and small business market.

1 That is a market that I think we have to pay
2 particular attention to in this discussion of combinations
3 of elements, given that the goal is to bring competition to
4 those markets and to consumers, and that is an area, I
5 think, that deserves specific scrutiny and specific
6 evaluation.

7 I would like to discuss today our view of what is
8 required to bring competition to those markets, our view of
9 how combinations of elements and specifically the ability to
10 combine any set of elements will allow competition to
11 flourish and under what terms, and then to finally discuss
12 briefly with you what MCI has done in that regard and how we
13 view that as a part of our overall company strategy.

14 First of all, I would like to outline what we
15 believe are the key requirements for competition to flourish
16 in the residential and small business arena. I think there
17 are three key things that need to occur. You have to be
18 able to achieve rapid and ubiquitous coverage. You need
19 that for scale in your marketing efforts and scale in your
20 operations. When you deal with the small end of a
21 marketplace, you need volume in order to make that market
22 sustainable.

23 Secondly, you need a clear incentive for companies
24 to compete for service in that marketplace. That must be an
25 economic incentive that allows for a broad and large market

1 opportunity and an economically profitable way to enter that
2 market. That is the business incentive behind what we are
3 talking about today.

4 Finally, because consumers and small businesses,
5 after all, have a very big role to play in this, you have to
6 bring to the marketplace something that is innovative,
7 something that is creative and compelling so that customers
8 have a reason to switch carriers. At that point, I think
9 you see that competition has delivered the benefits it
10 promises.

11 So how do combinations meet those objectives?
12 Really in any sense use of combinations in building for
13 competition meets all of the objectives of true competition.
14 For rapid and ubiquitous coverage, by using existing network
15 elements carriers are able to quickly achieve coverage that
16 allows them to get to the scale of marketing and operations
17 that is required.

18 You can reach consumers in a broad range of
19 geographic territories, rural, urban, etc., and you can
20 reach large segments of customers, both heavy users of
21 telecommunications services, as well as smaller users, so
22 you achieve that breadth of coverage by using existing
23 elements.

24 The market entry incentive can exist. There is
25 ability to reach a broad market, including the market for

1 access, which is an important component of the local service
2 marketplace. It also allows for focused investment,
3 investment in the things that will matter to the market as
4 it evolves over time, so investment of capital as a business
5 decision is made in a way that allows for the appropriate
6 development of facilities and networks that compete with the
7 existing combinations of networks.

8 Finally, it allows a carrier freedom from the
9 existing constraints of our BOC developed products and
10 services. It allows carriers to bring innovation
11 immediately to the marketplace through new and creative ways
12 to package local service, so I think you can find that it
13 meets every one of those objectives.

14 It is not sufficient to say that a carrier can
15 purchase or lease from the RBOC any set of elements,
16 although we believe that is a prerequisite for competition
17 to exist for residential and small business. The pricing
18 for those elements must be appropriate and cost based.
19 There must be no extraneous charges associated with use of
20 those leased elements.

21 In addition to the pricing, there need to be
22 standardized and scaleable support systems. Consumers
23 expect the experience of switching carriers for local
24 service to be very similar to what they expect today in long
25 distance. It happens quickly with no disruption of service.

1 There is an easy and effective way to make my choice
2 implemented in the marketplace.

3 Finally, we need to insure that there are
4 standardized performance standards, penalties and
5 appropriate incentives for the transactions to occur in a
6 parity environment for all carriers, including competitors.

7 Where the right conditions exist, MCI's strategy
8 is to use combinations of elements, including a combination
9 of all elements or platform of elements, to rapidly enter
10 the local market. Where the pricing is appropriate and
11 where the capability exists to enter those markets, we will.

12 We believe that combinations of elements is the
13 first step on the continuum of facilities based local
14 service. As we can build out to consumers, we will do so
15 with our own network and our own facilities, replacing as
16 appropriate elements that we have leased in the past from
17 the existing local carriers.

18 It helps us to evolve our strategy by allowing us
19 quickly to enter the local market and provide competition
20 for residential and small business customers and over time
21 build our facilities network to achieve coverage of the same
22 degree.

23 MCI has already invested nearly \$2 billion in
24 building our facilities. We will continue to do that, and
25 with the merger of MCI and WorldCom will immediately have a

1 presence that allows us to begin to reach consumers and
2 small business. Again, combinations of elements is an
3 essential first step in our strategy to reach consumer and
4 small business customers through a facilities based
5 strategy.

6 Thank you very much.

7 MR. SALEMME: Thank you very much. My name is
8 Gerry Salemme. I am with NEXTLINK Communications, and I am
9 here on behalf of ALTS, the Association of Local
10 Telecommunications Services. NEXTLINK I think is typical of
11 the entrepreneurial facility based carriers that compose
12 ALTS.

13 We were founded by Craig McCaugh, the cellular
14 pioneer, and on July 4, 1996, we initiated service in four
15 markets. Today we are currently providing facility based
16 service in 28 markets. Those range in size and demographics
17 from Spokane, Washington, and central Pennsylvania, very
18 small and rural, to some of the larger cities in the United
19 States, including LA and Los Angeles.

20 We are not resellers. We are facility based
21 providers. We invest hundreds of millions of dollars,
22 billions of dollars, as Keith has pointed out, in putting
23 facilities in the ground, switches, fiber, so that we really
24 can provide long-term, sustainable competition to the
25 currently monopolistic ILEC services.

1 We also believe that we have the right target
2 markets. We are looking currently at NEXTLINK at a small
3 business customer with five to 50 lines, but other ALTS
4 members are looking at different segments of the market,
5 including residential markets and larger corporations. We
6 believe that a facility based provider can be the long-term
7 solution to the competition that was required and looked for
8 in the Telecommunications Act of 1996.

9 I would like to make three key points, though,
10 that really I believe will capture what we are attempting to
11 accomplish today, which is to, one, again reiterate that the
12 best form of competition is facility based competition.
13 That is the greatest potential to really providing the
14 sustainable, differentiated service to the American
15 consumers in every market segment.

16 Second, access to unbundled loops in certain
17 combination of unbundled network elements is not only
18 statutorily required, it is critical to the development of
19 competition. It is the only way we are going to get the
20 breadth and reach of competition that we have heard talked
21 about in the Act.

22 Finally, the statutory distinction between
23 combination of unbundled network elements, the UNE, as
24 purchased or provided under Section 251(c)(3) and total
25 service resale as provided under Section 251(c)(4) of the

1 Act, that distinction must be maintained. There is a
2 statutory distinction, as the Eighth Circuit has found, and
3 that must be maintained.

4 As I said, we believe that the key to competition
5 is to have facility based providers putting facilities in
6 place and providing differentiated service. It is the way
7 to provide a customized service to the customers. It is a
8 way to insure that you can provide service at a lower cost
9 than is currently provided by the incumbent local exchange
10 carriers. We believe it is the best way to fulfill the goal
11 of the Act.

12 We are going to let Keith do our next investment
13 analyst show. He has all the facts down. I would actually
14 say there is probably \$18 billion that has been invested in
15 the market. One of the things that Keith did not point out,
16 though, is that is actually debt. As Craig McCaugh reminds
17 us every day, that is his entrepreneurial risk.

18 With the other members of ALTS, we have gone to
19 that marketplace, paid interest a heck of a lot higher than
20 any ILEC is paying for their debt because we are a risk
21 oriented business trying to get into the market, trying to
22 establish ourselves, trying to compete.

23 The most essential element for us to compete is
24 the unbundled loop. People can deploy switches. People can
25 ultimately build out transport, but it is virtually

1 impossible to replicate the unbundled loops that have been
2 put in place by the ILECs over a hundred years of monopoly
3 service. They are the choke hold that must be broken if you
4 want to have local competition to exist.

5 We cannot build all of those ourselves. Facility
6 based providers utilize combination of networks often to get
7 to those unbundled elements. For instance, we have
8 something called an extended loop in some markets where we
9 buy an unbundled loop and combine it with transport so we
10 can reach customers at central offices we are not physically
11 collocated.

12 If you take the current situation, the current
13 cost and time that we wait to get physical collocation, it
14 is essential to have this type of offer available to us. If
15 not, we are not going to get unbundled loops without being
16 caught in an endless loop, a vicious circle, in which we are
17 told you first have to collocate at a site to get that
18 unbundled loop.

19 We are second told that collocation space is not
20 available. I can give you example after example in every
21 market in the United States where we have run into this
22 problem. I have a letter from PacBell that recently came
23 out initially on January 30. They say there is no space,
24 total exhaustion in 59 central offices, including some of
25 the largest central offices in that California market. We

1 then get a second letter April 24, fully a year after we
2 have applied for space in some of these physical
3 collocations, saying miraculously they have resurveyed, and
4 they found space.

5 That is the type of thing that prevents us from
6 getting access to those unbundled loops, prevents us from
7 providing service to those customers. We need to break that
8 vicious circle. One of the things that the RBOCs have --

9 MS. MATTEY: Gerry, let's save some of these
10 specifics perhaps until the later panel when we get into
11 collocation, okay?

12 MR. SALEMME: Okay. Sorry.

13 MS. MATTEY: Why do you not finish up?

14 MR. SALEMME: Okay. The RBOCs right now, in our
15 minds, are misconstruing the Eighth Circuit decision on
16 combinations to say that they do not have to provide any
17 combination of unbundled network elements at all, that there
18 is no combination that is necessary. I think we just heard
19 Keith talk about that.

20 We believe the Eighth Circuit merely said that the
21 FCC could not require the provision of already combined
22 elements which resembled resold services at cost based rates
23 because this would obliterate the distinction that Congress
24 made between access to unbundled network elements under
25 Section 251(c)(3) and the purchase of wholesale rates of

1 ILEC retail services for resale under Section 251(c)(4).

2 I believe that this Eighth Circuit decision and
3 the attempt of the RBOCs underway is just a latest effort of
4 a just say no campaign. They are saying no to our ability
5 to get unbundled loops. We are not collocated. They are
6 just saying no to getting access to unbundled loops at
7 remote switches because that is against the combination
8 requirements of the Eighth Circuit decision; just say no to
9 getting unbundled loops at IDLC, integrated digital loop
10 carriers, because that will turn out to be a combination
11 that will not be permitted under their Eighth Circuit
12 interpretation.

13 We have got to somehow figure out how to break
14 this, how to insure the combinations are allowed, the
15 combinations that the FCC initially required, but to
16 continue to maintain the distinction that exists between
17 combining all the elements into the platform that Judy
18 talked about and total service resale, which is a different
19 pricing mechanism.

20 If we do that, I believe we can reach a happy
21 combination of competition in the market. We will encourage
22 facility based investment. We will encourage service to all
23 types of market segmentation, and we will be able to quickly
24 insure that the objectives of the 1996 Act are met.

25 Thank you.

1 MS. MATTEY: Thank you.

2 I would like to direct a question to all the
3 panelists. As Judy indicated, over time MCI's intention is
4 to transition to a facilities based entry strategy.

5 I would like any of the panelists to address the
6 question of what specifically needs to be in place before
7 that transition will occur. What do you need to have in
8 order to move from a use of the combination of elements to
9 our own facilities? Does anyone want to take a stab?

10 MR. TOWNSEND: I will go forward. The first thing
11 that is probably going to be needed is a decision from the
12 Supreme Court, it seems to me, because I think the Eighth
13 Circuit has probably, at least from the ILECs' perspective,
14 looked at the plain language of the statute and rendered a
15 decision which is consistent with that statute.

16 To the extent that an individual competitive
17 entrant, new entrant, makes business decisions, \$18 billion
18 worth of investment, as Gerry has updated us on, to promote
19 facilities based competition, that is part of competition.
20 That is part of the risk you take in the market.

21 To the extent that there are conflicting points of
22 view about what is required with respect to combination of
23 elements, as I said before, the Court is going to have to
24 make a decision about that, but there is no reason for
25 competing entrants to delay their business plans. We

1 already have a decision, and they can move in accordance
2 with that decision.

3 MS. MATTEY: Okay. Does anyone else want to add
4 anything?

5 MS. LEVINE: Absolutely. The use of the
6 combinations is a critical first step towards transitioning
7 to a full scale facilities based service for all customers.
8 We will continue to use the elements that are appropriate
9 from the RBOC over time, such as the unbundled loop, as a
10 means of access to our own intelligent network.

11 What needs to happen in order for a company to be
12 able to make that investment is, first of all, to achieve
13 some scale in operations and a set of customers, a customer
14 base, that is easily moved over to a set of services that is
15 primarily based on our own existing facilities.

16 The investment continues to occur because you have
17 a means in which to invest your additional capital and the
18 reach of your existing facilities to the smaller end of the
19 customer marketplace. Over time that obviously is allowed
20 to flourish, but if you think about the amount of time that
21 has passed already and the scale of investment already
22 placed within the network and yet the lack of competition
23 for the residential and small business marketplace, it is
24 obvious that you need to have a first transitional step in
25 order for competition to begin to take hold.